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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

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RENZ D. JENNINGS
Chairman
MARCIA WEEKS
Commissioner
CARL J. KUNASEK
Commissioner

IN THE MATTER OF COMPETITION
IN THE PROVISION OF ELECTRIC
SERVICES THROUGHOUT THE STATE
OF ARIZONA

Docket No. U-0000-94-165

COMMENTS OF PHELPS DODGE MORENCI, INC. IN RESPONSE TO
COMMENTS BY ARIZONA ELECTRIC POWER COOPERATIVE, INC,
NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION, RURAL
UTILITIES SERVICE, NATIONAL RURAL UTILITIES COOPERATIVE
FINANCE CORPORATION AND TRICO ELECTRIC COOPERATIVE

Phelps Dodge Morenci, Inc. ("Phelps Dodge") is one of 100,000 electric power consumers of Arizona rural electric cooperatives that could be denied access to lower-cost electric power if the comments of Arizona Electric Power Cooperative, Inc, National Rural Electric Cooperative Association, Rural Utilities Service, National Rural Utilities Cooperative Finance Corporation and Trico Electric Cooperative (collectively "electric cooperative entities" or "coop entities") are accepted by the Commission. Accordingly, Phelps Dodge offers the following response to some of the arguments made by these electric cooperative entities.

While each of these entities pays lip service to support for competition, at root, each of the entities requests that the 100,000 customers of Arizona electric cooperatives be precluded from the benefits of competition. This is bad public policy. Excluding cooperatives from competition would create large transmission islands of absolute monopolies within Arizona, stifling the public interest of providing lower cost electricity to consumers. As the entities note, the purpose of both the Rural Electrification Act and the Rural Electrification Loan Restructuring Act of 1993 was to ensure that

1 rural electric power consumers enjoy dependable and low-cost electricity. The electric cooperative
2 entities, however, would now have this Commission turn this purpose on its head: They all rely
3 on the federal government's historic role in rural electrification as a justification for preventing
4 electric utility customers from receiving the lowest possible price for electricity. Simply put, if the
5 electric cooperative entities get their way, rural consumers will be the only consumers in Arizona
6 prohibited from purchasing low-price electricity. Rather than acting to lower electrical costs, the
7 entities seek this Commission to allow the rural cooperatives to maintain monopolies that will
8 charge above-market rates for electricity.

9 On behalf of itself and the 100,000 other residential and industrial customers of rural electric
10 cooperatives, Phelps Dodge urges the Commission not to exempt (or delay subjecting) cooperatives
11 from the Commission's electric competition rules. In evaluating the comments of the electric
12 cooperative entities, this Commission should focus on what is in the best interests of electric
13 consumers, rather than the often artificial and contrived institutional interests of the cooperatives
14 themselves. Indeed, none of the specific comments of the electric cooperative entities justify
15 exempting cooperatives from competition.

16 First, the coop entities claim that restructuring threatens the federal tax exempt status of
17 AEPCO and Arizona's distribution rural electric cooperatives. The coop entities have not
18 demonstrated, however, either (i) that any electric cooperative would actually lose their tax exempt
19 status or (ii) that the cooperatives could not restructure to prevent the loss of the tax exempt status.
20 At best, the entities offer speculation that is belied by both the facts and common sense. For
21 example, it would appear that cooperative bylaws could be amended to establish different classes
22 of membership so that a third-party power supplier or marketer could simply become a member of
23 the cooperative. Consequently, any transmission fees paid by such a member to the cooperative
24 would be considered revenues from members and would not run afoul of the 15% requirement.
25 Interestingly, the State's only operation and transmission cooperative, Arizona Electric Power
26 Cooperative, Inc., has utilized precisely this structure to create different classes of membership so

1 that revenues derived from the City of Mesa (a Class B member) and Salt River Project (a Class
2 C member) are member revenues for federal income tax purposes.

3 More fundamentally, the electric cooperative entities fail to explain why the loss of tax
4 exempt status will necessarily harm its member consumers. Whether or not the loss of tax-exempt
5 status will result in a large corporate tax depends on the operation of the cooperative. If
6 cooperatives continue to operate on a break-even basis, any tax will be de minimis. Moreover,
7 even if the cooperatives pay a tax, consumers may still be better off because they would have
8 access to less expensive electricity.

9 Second, the coop entities argue that they should be exempt from competition because they
10 owe debt to the federal government. Specifically, they contend that the proposed rules could cause
11 a default of their obligations to the federal government because these obligations purportedly require
12 the cooperatives to have an exclusive service territory. This argument is also without merit.

13 Electric cooperatives are hardly unique in owing debt--virtually all electrical utilities owe
14 debt. As with the cooperative's debt, lenders advanced funds to electric utilities at a time when
15 the utilities were regulated monopolies with an exclusive service area. The fact that the
16 cooperatives' debt is from the federal government rather than from private sources hardly justifies
17 denying rural cooperative customers--but not customers of other utilities--the opportunity to
18 purchase low cost electricity.

19 In any event, there is substantial reason to doubt the entities' claim that they would be put
20 into default. Nothing in the Rural Utility Services ("RUS") mortgage that requires cooperative-
21 borrowers to maintain "exclusive service rights." Article III, Section 1(g) of the RUS mortgage
22 requires the mortgagor to maintain its corporate charter or franchises, permits, easement or licenses
23 required to carry on its business. None of these conditions confer "exclusive territorial service
24 rights."

25 Third, the coop entities argue that the draft rules would require that the federally supported
26 cooperatives' facilities be made available to companies that are not the intended beneficiaries of the

1 Rural Electrification Act. Yet, as noted by the National Rural Electric Cooperative Association
2 itself (NRECA Comments at 11 n.8), RUS regulations do not preclude such use of RUS-funded
3 facilities as long as the primary purpose of the loans remains to furnish or improve service to
4 intended beneficiaries. That test would be satisfied here--regardless of who generates the electric
5 power, the ultimate consumer of the electric power transmitted over cooperative facilities will be
6 the existing cooperative members/consumers.

7 Fourth, the coop entities argue that cooperatives should be exempt from the proposed
8 regulations because municipalities are excluded. This ignores that municipalities are exempted only
9 because the Commission lacks jurisdiction over municipalities--not because of any reasons of public
10 policy. Cooperatives, on the other hand, are public service corporations over which the
11 Commission exercises plenary rate making and general service jurisdiction. Moreover, rural
12 electric cooperatives play a far larger role in providing transmission services in Arizona than do
13 municipalities. Accordingly, the inclusion of rural cooperatives is more important to the success
14 of statewide electric competition. Exempting rural cooperatives would create islands of monopoly
15 that could stifle transmission of competitive electricity to other Arizona consumers.

16 In addition to seeking an outright exemption from competition, the electric cooperative
17 entities seek special cost recovery rules that would effectively eliminate the opportunity for rural
18 electric customers to benefit from low-cost competitive prices for electricity. For example, the
19 coop entities propose that the Commission be required to allow unmitigated stranded cost recovery
20 without a specified time limit. These cost recovery proposals are unworkable, unnecessary and
21 serve to defeat the very policy objectives that competition will promote. Mitigation and collection
22 of stranded costs during a minimum period of time is essential to the implementation of
23 competition. Without mitigation of stranded costs, incumbents can obtain windfall profits and
24 create large barriers to market entry. This is because unwarranted stranded cost recovery charges
25 levied on competitive prices effectively will scuttle the opportunity for real competition.

26 . . .

Moreover, whether departing customers should be required to pay stranded costs should be determined on a case-by-case basis. For example, many longstanding customers will have already paid sufficient revenue to allow full amortization of the facilities used to provide service to them. Simply put, in such cases, there are no stranded costs to recover. Similarly, it is unlikely that any distribution cooperatives can claim stranded costs. The distribution system of the cooperative will be used regardless of who generates the electricity used by consumers.


In conclusion, Phelps Dodge urges the Commission to adopt rules that will ensure all Arizona electric consumers the opportunity to benefit from competition. Arizona's 100,000 rural electric cooperative consumers should not be deprived of the benefits of competition. Accordingly, the Commission should include rural electric cooperatives within the rules, and reject the electric cooperative entities' proposals on stranded cost recovery.

October 3, 1996.

Respectfully submitted,

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Original and ten (10) copies of the foregoing filed this 3rd day of October, 1996, with:

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